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C O N F I D E N T I A L SECTION 01 OF 03 BUDAPEST 000628

SIPDIS

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TAGS: [ENRG](#) [ECON](#) [EPET](#) [PGOV](#) [RU](#) [UK](#) [HU](#)
SUBJECT: STORING UP GAS FOR ANOTHER WINTER CUTOFF

REF: A. BUDAPEST 30
[1](#)B. BUDAPEST 356

Classified By: Economic Officer, Jeffrey M. Jordan, reasons 1.4 (b,d)

[1](#)1. (SBU) Summary: Hungary is nearing the completion of a significant addition to its already extensive natural gas storage capacity. This new capacity will further enable gas to continue flowing to consumers in Hungary and possibly to neighboring countries in the event of a cutoff similar to that of January 2009. Gas injection at Hungary's new strategic gas storage site, however, is facing delays due to the fact that Emfesz, the controversial gas trader that won the tender to supply the facility, still lacks a steady gas supply. Some industry insiders see Gazprom's efforts to secure gas storage capacity west of Ukraine as portending another gas conflict this winter. Should this occur, Hungary appears well-prepared to meet peak demand for at least one month and considerably longer at reduced levels. End summary.

[1](#)2. (SBU) EconOff met with Istvan Kutas, company spokesman for E.On Hungaria (E.On), Hungary's largest natural gas supplier and commercial storage operator, and Dr. Gabor Szorenyi, Director of Electricity, Gas and District Heating Licensing and Monitoring and Consumer Protection at the Hungarian Energy Office. The discussions focused on Hungary's progress in replenishing its natural gas storage reservoirs prior to winter. Hungary's extensive gas storage capacity, along with the ability to reorient gas imports via Austria's Baumgarten gas hub, proved essential to limiting the January 2009 gas cutoff's impact to rationing measures imposed on large industrial consumers. Hungary was also able to provide modest gas exports to neighbors in the Balkans. Although Hungary fared better than its neighbors to the south, it quickly became clear that it would need additional storage capacity to weather a protracted gas cutoff (ref A).

E.ON ADDS GAS STORAGE CAPACITY

[1](#)3. (SBU) E.On is nearing the completion of a 600 million cubic meter (mcm) expansion of its Zsana gas storage facility, one of its five storage sites, increasing E.On-owned commercial storage capacity to 4.3 billion cubic meters (bcm). As a result of the expansion, the average daily withdrawal capacity will increase by 4 mcm/d to about 55 mcm/d, enough to cover roughly 70 percent of daily demand during periods of peak consumption. E.On estimates that it

can sustain gas withdrawals at the peak rate for about 10-14 days, after which, due to the drop in pressure, it can continue withdrawing at about 80-90 percent of the peak rate for about 20 days. According to Kutas and Szorenyi, Hungary's gas marketing companies waited until late July, when wholesale gas prices were scheduled to drop, to begin purchasing gas for winter storage. E.On is now injecting gas into the reservoir at the maximum rate, which should peak at 33 mcm/d when the Zsana expansion is completed in mid-September. Kutas expects the reservoir to be completely filled by late October.

STRATEGIC GAS RESERVE FACES DELAYS

14. (SBU) Hungarian oil and gas giant MOL, in a joint venture with the Hungarian Hydrocarbon Stockpiling Association, is nearing the completion of a new gas storage facility at the depleted Szoreg gas field with a dedicated pipeline from Ukraine to feed into it. The facility's 1.9 bcm capacity will include 1.2 bcm for strategic storage, scheduled to begin operation in January 2010, and 700 mcm in commercial storage, operable from March 2010. The strategic stock will guarantee Hungary an additional 20 mcm/d for 45 days in the event of a gas crisis. The facility's peak withdrawal capacity is expected to reach 25 mcm/d, including the quantities available for commercial use.

15. (C) According to recent press, gas injection at Szoreg is facing some delays. Technical problems with the compressors and pipelines have held things up by a few weeks. According to Kutas and Szorenyi, however, the real cause of the delay

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is that Emfesz, which had previously won a tender to fill the strategic reserve at Szoreg, lacks the gas needed to fulfill this contract. Emfesz claimed to have a new gas supply agreement with Rosgas after the termination of its supply arrangement with Rosukrenergo and its controversial acquisition by Rosgas (ref B), but the gas has yet to materialize. As such, Emfesz continues to purchase gas from E.On on a week-to-week basis--at a price well above what Emfesz charges to its clients--to keep its commercial and residential customers supplied, but it has not secured a source of gas to meet its commitment to fill Szoreg. (Note: Kutas mentioned that after a recent increase in the price E.On charges Emfesz, E.On received a letter from Emfesz conveying an "order" by the Ministry of Transport, Telecommunication and Energy to restore the price to the initial level "in the interest of national security." E.On apparently complied. End note.)

16. (C) Emfesz had to scrap plans to begin supplying gas to Szoreg by August 15 and now claims it will begin injection by August 31, still plenty of time to meet the legal deadline to fill the strategic storage reserve by December 31. Kutas, however, cites an "industry rumor" that Emfesz and MOL plan to offset Emfesz' obligation by reclassifying 700 mcm of so-called "cushion gas," already present in the reservoir and used to maintain pressure, as strategic storage gas. (Note: Kutas leaked this information to several local news outlets, but only one, economic daily Vilaggazdasag, printed it. Kutas attributes this to a general media aversion to printing negative news about MOL. End note.) MOL publicly denies this and claims that all preparations are going according to plan.

17. (C) In addition to Emfesz' apparent difficulty fulfilling its strategic storage obligation, Dr. Szorenyi says the Hungarian Energy Office is generally concerned about the likelihood that Emfesz will still be without a long-term supplier at the onset of winter. According to Szorenyi, the Energy Office is prepared to revoke Emfesz' license and send its customers, including the supply contract for the strategic storage facility, to E.On if the situation is not resolved in due time. He indicated that injection at Szoreg would need to begin by early October at the latest to ensure

available supply by January.

GAZPROM DESPERATELY SEEKING STORAGE

18. (C) Kutas commented on recent reports that Gazprom is actively seeking to lease storage capacity downstream from Ukraine and posited that Gazprom's efforts to stockpile gas closer to its European customers suggests that it might be preparing for another gas cutoff this winter. E.On's own industry sources, however, believe a gas crisis is unlikely this winter because Gazprom, already under some financial strain, cannot bear the loss of cash flow.

19. (C) Gazprom is reportedly interested in booking 100-200 mcm of storage capacity in Hungary to ensure supplies to its Balkan customers, who were severely impacted by the gas cutoff last January. According to Kutas, after learning through the press about recent talks in Vienna between Gazprom and Srbijagaz on directly contracting with E.On for storage in Hungary, E.On informed the parties that capacities would be allocated based on a public auction. E.On plans to auction off storage space in tranches, with initially-planned offers of 40 and 90 mcm tranches beginning in late August and early September, respectively, as the new capacity is gradually brought online. This also allows E.On to take advantage of probable increases in market rates as storage capacity becomes more scarce and winter approaches.

110. (C) In a brief follow-up conversation, Kutas reported that Gazprom has since told E.On it is in direct negotiations for storage space at a separate site in Hungary, most likely the new storage site at Szoreg. Kutas believes this is a bluff, however, given the project's delays and the fact that the commercial storage portion is not scheduled to begin operating until later this winter, ostensibly too late to be of any use in a gas cutoff.

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GOH TO REFINE CRISIS MANAGEMENT PLAN

111. (SBU) Parliament is also set to vote soon, albeit somewhat belatedly, on legislation to update Hungary's gas crisis management plans, including incentives for large consumers to enable rapid fuel switching from gas to oil, obligatory provisions for gas marketers to book commercial storage, clarification of the rules on use of the strategic stockpile, and a modification of consumer rationing measures.

An important revision to the rationing rules will allow industrial consumers enough gas to heat their facilities and protect plant and equipment, even if required to shut down production.

HUNGARIANS UNLIKELY TO FREEZE IF THE GAS STOPS FLOWING...
TEMPORARILY

112. (C) Comment: Hungary appears to have put some of the lessons from recent years' gas crises into practice. With ample storage capacity to meet daily demand needs, depending on the temperature, for about a month without significant rationing, Hungary is unlikely to be left in the cold in the event of another wintertime gas shortfall. In addition to this near 50-percent increase in gas storage over last year, Hungary's domestic gas production (9 mcm/d) and pipeline link to Austria (up to 12 mcm/d) further enhance Hungary's ability to weather a short-term crisis. Plans currently underway between MOL and its regional partners to establish pipeline interconnections with neighboring Romania (2010), Croatia (2011), and Slovakia (2015) will offer an expanded range of options for keeping gas flowing amid future cutoffs. Yet, such measures are no substitute for source diversification. With roughly 80 percent of its gas coming from Russia or through Gazprom-controlled pipelines and with natural gas comprising over 40 percent of its primary energy supply, Hungary will remain highly vulnerable to disruptions in the supply or Russian gas. End comment.

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